

The State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. See Ill. Adm. Code 130.220. (This is a PLR).

March 20, 2000

Dear Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (see enclosed), is in response to your letter of November 5, 1999 and the powers of attorney we received on December 28, 1999. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to #101, #202, #303, #404, COMPANY, BUSINESS, and CORPORATION for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither #101, #202, #303, #404, COMPANY, BUSINESS, or CORPORATION nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter, you have stated and made inquiry as follows:

I am writing to you requesting a Private Letter Ruling (PLR), pursuant to 2 Ill. Admin. Code Sec. 1200.110, addressing whether any one of a series of virtually identical private express trusts (specifically, #101, #202, #303, and #404) is liable for Retailers' Occupation Tax (ROT) or Use Tax (UT) on its business transactions occurring from July 1, 1996 to the present. PLRs respond to inquiries made by taxpayers or their representatives under power of attorney (attached). We understand that PLRs discuss tax principles and are binding on the Illinois Department of Revenue (IDOR) to the extent that the material facts of the situation remain the same, and the law relied upon in the ruling does not change.

FACTS

1. The Business Organization

Each of these trusts was organized and functions as a grantor trust under the common law of the STATE. They are in the auto-leasing business. Their trustee, BANK, utilizes an agent, COMPANY, to manage their respective businesses. The agent does the billing, purchasing, and collecting for the trustee. Although true ownership of the vehicles lies with the trust, the agent holds title as agent for the trustee to all leased vehicles. Once title transfers to the agent for the trustee, the agent holds the title for the duration of ownership. Each trust has one investor/beneficiary, who contributes funds to it. (COMPANY is the beneficiary of #101. BUSINESS is the beneficiary of both #202

and #404. CORPORATION is the beneficiary of #303.) The trustee, through its agent, then uses the funds to finance auto-leasing transactions.

2. The Auto-Leasing Transaction

The auto-leasing transaction has the following steps:

- A customer wants to lease a new car, which is titled to a car dealer. The dealer purchased the car tax-free by issuing to the car manufacturer an Illinois resale certificate. The dealer is not primarily engaged in the business of leasing.
- The car dealer sends the customer's credit application to the agent's office.
- Once the agent approves the application, the customer signs a lease agreement with the dealer as lessor.
- The lease is always for a term greater than one year. It is a true lease and not a conditional sale.
- The lease agreement clearly states that the dealer/lessor will immediately assign the lease to the agent.
- The dealer is registered with the IDOR as a retailer.
- The dealer collects, under contractual agreement with the customer/lessee, sales tax measured by the car's selling price and remits tax to the state.
- As agent for the trustee, the agent uses the trust's capital to purchase the car for its selling price.
- The car becomes titled to 'COMPANY as Agent' of the trustee, and the agent obtains from the Secretary of State certificate of title to the car.
- The dealer immediately assigns the lease to the agent, who reassigns it to the trust.
- The trustee, through its agent, receives the stream of lease payments from the customer/lessee and then remits the payments to the investor/beneficiary,
- If the customer/lessee chooses to buy the car at the end of the lease, it pays to the agent the buyout amount that approximates the car's current fair-market value. (Alternatively, the buyout amount might be a pre-established fixed-price purchase option measured by a current estimate of the car's end-of-lease fair-market value.)

- The agent, who is an IDOR-registered retailer, collects sales tax on the buyout amount and remits it to the state.
- If the lessee/customer does not choose at the end of the lease to purchase the car, the agent sells it to an auction house. The agent obtains at point of sale the auction house's Illinois resale certificate. The auction house then sells the car to another dealer.

3. Sale of an Interest in the Trust

A beneficiary/investor may sell its interest in the trust. When a sale of an interest occurs, the identity of the beneficiary changes. However, title to and ownership of the leased cars remain with COMPANY as agent for the trustee. Moreover, the agent continues to manage the leases, which remain with the trust. The customer/lessee remains the same, and it likewise retains its option to buy the automobile at the end of the lease for fair-market value. In other words, when a sale of an interest occurs, except for a change in the beneficiary/investor of the trust, the leasing business continues as usual.

ISSUES

- Since the dealer is initially listed as lessor on the lease agreement, do the subsequent assignments of the lease, first to COMPANY and then to the trust, result in imposition of sales tax?
- Is sales tax imposed when a beneficiary sells its interest in the trust?

STATEMENTS

No audit or litigation is currently pending between the trust and the IDOR. To the best of our knowledge, the IDOR has not previously ruled on the same or similar issue for the trust, nor has the trust submitted a petition on a similar issue and withdrew it before a letter ruling was issued. The IDOR did issue a General Information Letter (GIL) on these issues, which has been enclosed.

LAW

Illinois imposes the Retailers' Occupation Tax (ROT) on persons selling at retail tangible personal property. 35 ILCS 120/2. 'Sale at retail' is defined as the transfer for consideration, and not for resale, of title to or ownership of tangible personal property. 35 ILCS 120/1. Illinois also imposes use tax (UT) on the privilege of using in the state tangible personal property purchased anywhere at retail. 35 ILCS 105/3. The UT compliments the ROT. 86 Ill. Admin. Code Sec. 150.101(c).

Illinois recognizes two types of leases: conditional sales and true leases. A conditional sale is a lease that results in the lessee paying a nominal amount or one dollar at the end of the lease term for ownership of the item leased. Conditional sales guarantee at the time of the lease that the leased property will be sold. True leases, on the other hand, either have no buyout provisions or require the lessee to pay the fair market value of the item at lease end to purchase the item leased. IDOR GIL ST 99-0169.

In true lease situations, Illinois imposes the UT upon lessors because they are considered the end users of tangible personal property purchased for lease. 86 Ill. Admin. Code 130.220(a) and 130.2010(b). Trusts in Illinois are subject to the UT if they are in the business of leasing tangible personal property in the state. Dealers, which sell cars to trusts, along with assigning auto leases to them, are liable accordingly for the ROT on the selling price of the car¹. PLRs ST 91-0372 (5/13/91), 93-0510 (8/6/93), and 96-0424 (10/16/96). Leases of automobiles for a duration of one year or less are subject to taxation under the Automobile Renting Occupation and Use Tax Act. 86 Ill. Admin. Code Sec. 180.101(a).

Illinois allows for an interim use exemption from UT when a retailer uses items held for sale but keeps the items as inventory on its books during the period of use. The IDOR applies the interim use exemption from the UT to tangible personal property leased by persons which primarily sell the tangible personal property at retail. To claim the exemption, the lessors must also keep the leased property on the books as inventory during the period of the lease. 86 IL Admin. Code 150.306(a)(1)&(2).

A lessor will owe at the end of the lease ROT on the buyout amount if it sells the car to the lessee. It will not owe ROT if it sells the car for resale and obtains at point of sale from the buyer a properly-executed resale certificate. 35 ILCS 120/1(c), 86 Ill. Admin. Code Sec. 130.1405, and PLR ST 91-0372 (5/13/91).

An IDOR regulation states that the ROT does not apply to sales of intangible personal property. 86 Ill. Admin. Code Sec. 130.120(a). The regulation cites evidences of interests in property as examples of intangible personal property. The IDOR has also stated that the sale of an interest in a trust, without a corresponding transfer of tangible personal property, is a sale of intangible personal property not subject to the ROT. GIL ST 94-0537 (11/7/94), and PLR ST 96-0424 (10/16/96). Furthermore, assignments of leases, without an accompanying transfer of tangible personal property, are considered sales of intangible personal property exempt from the ROT. PLRs ST 90-0232 (5/29/90), 90-0573 (7/31/90), and 96-0424 (10/16/96).

ANALYSIS

The transactions involved in the factual situation described above amount to a true lease under Illinois law. The buy out provision given the lessee at lease end is for the full fair-market value of the car. Furthermore, all lease terms extend beyond one year. Therefore, the lessor should normally be liable for the UT when the lease agreement is

made with the lessee. However, no tax is due in this case because the lessor may properly claim an interim use exemption from the tax.

ROT is only due when the dealer assigns the lease agreement to the agent. This is because a transfer of title to and ownership of the vehicle accompanies the assignment. The dealer pays the ROT due the IDOR ². The agent of the trust does not owe further tax on the subsequent assignment of the lease agreement to the trust.

The agent would collect UT from the lessee/customer should it decide to buy the car at the end of the lease. The taxable base would be the buyout amount. However, no UT would be due from the purchaser if it tendered at point of sale a properly-completed Illinois resale certificate, such as in the case of a sale to the auction house.

The sale of a beneficial interest in the trust would be exempt from the ROT because a transfer of title to or ownership of tangible personal property does not accompany the sale. In other words, when the beneficiary sells its interest in the trust, the leased vehicle remains titled to the agent of the trustee. Thus, the sale is one of intangible personal property not subject to the ROT. Likewise, the assignment of the lease from the agent to the trust is exempt from ROT because no transfer of title to or ownership of tangible personal property accompanies the assignment. Therefore, it is considered a sale of intangible personal property exempt from the ROT.

CONTRARY AUTHORITY AND DECISION

The dealer's initial execution of the lease and then its assignment to the agent may be considered two distinct taxable events. In other words, the dealer, as the initial lessor, might incur one UT and the agent, as the subsequent lessor, might incur another UT. However, even if two distinct events are found to occur, the first event, when the dealer becomes lessor of the car, is not subject to tax under the interim use tax exemption because the dealer is in the business of selling cars and keeps the car as inventory subject to sale during its term of use. In other words, motor vehicle dealers which enter into leases of motor vehicles in order to make a contemporaneous sale of the vehicles may claim the interim use exemption.

The sale of the beneficial interest in the trust would only result in a taxable event if the beneficiary transferred tangible personal property along with the sale of the interest. However, under the facts as stated, no tangible personal property is conveyed when the beneficial interest of the trust is sold. There is likewise no taxable event when the agent assigns the lease to the trust, as no tangible personal property accompanies the assignment.

CONCLUSION

The facts of this case support the finding that the dealer and the agent meet their respective ROT/UT obligations on the lease transaction when the dealer remits ROT to

the state based on the selling price of the car. This conclusion is consistent with state law and prior IDOR rulings.

The facts of this case also support the finding that the sale of the beneficial interest in the trust would be a sale of intangible personal property beyond the scope of the ROT/UT. The transfer of the lease from the agent to the trust would also be exempt as the transfer of intangible personal property. Both conclusions are consistent with state law and prior IDOR rulings.

We request that the IDOR issue a PLR addressing the issues presented. Your cooperation is appreciated.

For purposes of this Private Letter Ruling, we are assuming that #101, #202, #303, and #404 (grantor trusts) are recognized as valid legal entities under Illinois law. The Department considers a valid trust to be subject to the Retailers' Occupation Tax Act and the Use Tax Act if it is in the business of leasing tangible personal property in Illinois. We are also assuming that the leases referenced in your letter are true leases (not conditional sales) and that the leases are not subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

We cannot provide you with a binding answer on the tax liabilities of persons, such as the car dealers, who are not a party to this Private Letter Ruling. There are generally two separate taxable transactions when a dealer leases a vehicle and then sells or "assigns" that vehicle to another entity. When a car dealer executes a lease with a customer for a vehicle (first taxable transaction), Use Tax is incurred by the dealer on the purchase price of that vehicle unless the dealer can document a valid exemption. When the car dealer sells or assigns that vehicle to another person or entity (second taxable transaction), the dealer incurs Retailers' Occupation Tax liability on that sale unless the dealer can document a valid exemption. The interim use exemption may be available to the dealer in regards to the first taxable transaction if that dealer is primarily engaged in the business of selling vehicles at retail. See the enclosed copy of 86 Ill. Adm. Code 150.306. The leasing of vehicles by a car dealer who is primarily engaged in the business of selling such vehicles at retail is within the interim use exemption if those leased vehicles are carried as inventory on the books of the retailer or are otherwise available for sale during the lease period. See subsection (a)(2) of Section 150.306.

The second paragraph of your letter entitled "The Business Organization" states that although true ownership of the vehicles lie with the trust, the agent holds the title for the duration of the ownership. Among the information listed in the "FACTS" section of your letter, you state that the vehicles become titled to "COMPANY as Agent" of the trustee, and the agent obtains the certificates of title for those vehicles from the Secretary of State's Office. Further, the information contained in the "ANALYSIS" section of your letter states that the assignment of the lease to the agent, COMPANY, accompanies the title to and ownership of the vehicle. The agent then subsequently assigns the leases to the trusts. This would indicate that ownership of the vehicles and the leases were transferred to the agent for the trustee and not to the trusts.

It was unclear from the facts contained in your letter whether the leases and leased vehicles purchased from the dealers were being purchased by the trustee, BANK, through its agent, COMPANY, or whether they were actually purchased by COMPANY on its own behalf with funds provided by the trustee. Based on the Vehicle Leasing Dealer Agreement we received from you on January 31, 2000, we understand that the dealers sell the leases and the leased vehicles to the trustee, BANK, through its agent COMPANY. The trustee, BANK is the owner of the leases and the leased vehicles. The leased vehicles are titled in the name of COMPANY as agent for the trustee, BANK.

The trustee, BANK then transfers or assigns to the trusts, through its agent, COMPANY, the leases purchased from the dealers. The trusts, #101, #202, #303, and #404 do not take title to the leased vehicles and have no ownership interest in those leased vehicles.

The sales of the leased vehicles by the dealers to the trustee, BANK, are sales of tangible personal property subject to Retailers' Occupation Tax and Use Tax liability. The dealers will incur Retailers' Occupation Tax liability on the gross receipts from those sales, and the trustee, BANK, will incur a corresponding Use Tax liability on the purchase price of the leased vehicles. A subsequent sale or "transfer" of those leased vehicles by BANK will result in a second taxable transaction.

If the trustee, BANK, subsequently transfers/sells the leased vehicles in Illinois, it will incur Retailers' Occupation Tax liability on the gross receipts from those sales unless it can document a valid exemption. See 35 ILCS 120/1c (1998 State Bar Edition). This would require the trustee, BANK, to be registered as a retailer in this State. Your letter states that the agent, COMPANY, is an IDOR-registered retailer and either collects sales tax on the "buyout" amounts and remits it to the State or sells the vehicles to auction houses and obtains resale certificates from the auction houses.

Which party incurs the tax in these situations will depend on whether the agent, COMPANY, is selling the vehicles on behalf of the trustee, BANK, as a disclosed principal or whether the trustee is an unknown or undisclosed principal. See the enclosed copy of 86 Ill. Adm. Code 130.1915 regarding the liability of agents acting on behalf of disclosed and undisclosed principals. From the facts in your letter regarding the language that appears on the title issued by the Secretary of State's Office, it looks as though COMPANY is selling the vehicles on behalf of the trustee, BANK, as a disclosed principal. When agents are acting on behalf of known or disclosed principals, the sale of the tangible personal property is taxable to the principal and not the agent if the principal is a retailer of the tangible personal property personal property being sold. If COMPANY is acting on behalf of the trustee, BANK, as a disclosed principal for the sales of the vehicles, those sales are taxable to BANK and not COMPANY. BANK must be registered with the Department and the tax must be paid under BANK's Illinois Business Tax number (IBT) number.

If our assumption is incorrect that COMPANY is selling the vehicles on behalf of the trustee, BANK, as a disclosed principal, then COMPANY is acting as a retailer and those sales are taxable to COMPANY and not the trustee, BANK. The trustee, BANK, may sell the vehicles to COMPANY without incurring tax as sales for resale.

If the subsequent assignments of the leases from the trustee, BANK, to the trusts, #101, #202, #303, and #404, do not include the transfer of the ownership of the leased vehicles, those assignments are not subject to Retailers' Occupation Tax or Use Tax liability because the assignments of the leases are considered transfers of intangible personal property.

When a beneficiary, COMPANY, BUSINESS, or CORPORATION sells all or part of its interest in one of the trusts and those sales do not include the transfer of the ownership of any leased vehicles or other tangible personal property, those sales are considered sales of intangible personal property and are not subject to Retailers' Occupation Tax or Use Tax liability.

We noted that some of the presumptions in your letter were incorrect. The information in dot point number 7 of part 2 of the Facts portion of your letter and footnote numbers 1 and 2 of your letter do not correctly describe the proper tax liabilities of the parties. Generally, lessors that purchase vehicles for lease or remove them from inventory for lease incur Use Tax liability on the cost price of the leased vehicle. The lessees incur no tax liability. However, the lessors traditionally contract with the lessees to require the lessees to reimburse the lessors for their Use Tax liability. In the situation described in your letter, the lessors/dealers may qualify for the interim use exemption and incur no Use Tax liability on the cost price of the leased vehicle. This would mean that the lessors have no Use Tax liability for the lessees to reimburse.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

I hope this information is helpful. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Terry D. Charlton
Associate Counsel

TDC:msk
Enc.

1 The auto dealer may reimburse itself for any ROT which it remitted to the IDOR by collecting UT from the customer/lessee (rather than from the trust). The dealer may collect the UT provided that it has contracted with the customer/lessee to do so. (The customer/lessee's obligation to pay the UT in this case is based on a contractual agreement with the dealer. Regardless of the contractual agreement, the dealer still remains legally obligated to remit the ROT to the state. Ibid.)

2 The dealer may reimburse itself for the ROT due with the UT paid under contractual obligation to it by the customer/lessee. The dealer need not collect any additional UT from the agent because the UT already collected is based on the selling price of the car.